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IN THE

Supreme Court of the United States

October Term, 1978
No. 78-1577

SEARS, ROEBUCK & CO., a corporation,
Petitioner,

vs.

COUNTY OF LOS ANGELES and CITY OF COMPTON,
Respondents.

Brief of Amicus Curiae, Pioneer Electronics of America, Soundesign Western, Association of Electronic Importers, Foreign Trade Association of Southern California, in Support of Petition for Writ of Certiorari to the Court of Appeal of the State of California, Second Appellate District.

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Interest of Amicus.

Pioneer Electronics of America, Soundesign Western, the Association of Electronic Importers, and the Foreign Trade Association of Southern California hereby respectfully file this Brief Amicus Curiae in Support of the Petition for Writ of Certiorari to the Court of Appeal of the State of California, Second Appellate District, filed herein by Sears, Roebuck & Co. The consent of the attorneys for Petitioner and for Respondents was obtained April 12, 1979, which letters of consent are respectively attached hereto as Exhibits "A" and "B."

Pioneer Electronics of America and Soundesign Western are domestic corporations importing goods into the State of California, a substantial portion of which is transshipped out of the State, and transshipment exemptions under California Revenue & Taxation Code Section 225 have been claimed, and such claims are pending before the County of Los Angeles and the courts of the State of California. These claims are dependent upon the outcome of this case.

Amicus Curiae Association of Electronic Importers is a California corporation consisting of electronic importers, all of whom have inventories in the State of California, transshipped a portion of such inventories out of the State, and fall within the provisions of Revenue & Taxation Code Section 225.

Amicus Curiae Foreign Trade Association of Southern California is a nonprofit association of more than 460 importing, exporting the service firms engaged in international trade and vitally interested in the impact and effect this litigation has had and will have on the importing industry and international trade. The members of the Association include more than 110 firms engaged in importing products from various countries throughout the world.

Attorneys for Amicus Curiae represent the above corporations and over 50 companies that have claimed transshipment exemptions under the provisions of California Revenue & Taxation Code Section 225 and have lawsuits pending against the County of Los Angeles for recovery of exemptions which have been denied. Said attorneys are familiar with all of the issues, briefs and facts in this case, represented Zee Toys, the companion case to *Sears, Roebuck & Co. v. County*

of Los Angeles, and can make a significant contribution to the Court's consideration of the Petition for Writ of Certiorari.

Amicus Curiae Pioneer Electronics of America and Soundesign Western are wholesalers, as distinguished from Petitioner Sears, Roebuck & Co., a retailer. To the extent such distinction is relevant, it is submitted that attorneys for Amicus Curiae can add to the consideration of the merits of this case.

Question Presented.

Whether California Revenue & Taxation Code Section 225, in granting a property tax exemption to imported inventories no longer in transit, but intended for transshipment out of the State of California, regulates interstate and foreign commerce and thereby violates the Commerce Clause of the United States Constitution.

Constitutional Provision Involved.

The constitutional provision involved is the Commerce Clause, Article I, Section 8, Clause 3 of the Constitution of the United States, which grants to Congress the right: "To regulate Commerce with foreign nations, and among the several States, and with the Indian Tribes."

Statement of the Case.

In 1975 the California Legislature determined that an exemption for distributors, both retailers and wholesalers, was necessary in order to encourage importers presently located in the State of California to remain, and to encourage other importers to locate in the State.

The Legislature enacted Revenue & Taxation Code Sections 225 and 225.1, which provided in part, an exemption on that portion of business inventories that was imported from foreign countries and destined for transshipment out of the State of California. An importer was entitled to exempt that percentage of the imported inventories represented by the ratio of the previous year's total sales or shipments compared to his out-of-state sales or shipments. A copy of relevant sections is attached as Exhibit "C" hereto.

Petitioner Sears, Roebuck & Co., as well as Amicus, maintained warehouses in the County of Los Angeles during the relevant tax years in question, claiming exemptions under the provisions of Section 225 for that portion of their imported inventory which was intended for transshipment out of the State. The County denied the exemptions on the grounds that a warehousing operation did not come under the exemption provided by the statute. The County of Los Angeles took the position that only goods actually in transit on a continuous journey were entitled to the exemption. Subsequently, and during the course of litigation, the County of Los Angeles took the position that the transshipment exemption was unconstitutional. No evidence was introduced by the County relating to any impact which the statutes might have upon commerce between the states or foreign nations.

REASONS FOR GRANTING THE WRIT.

A. The Court of Appeal Has Decided a Federal Constitutional Question of Substance in a Manner Contrary to Applicable Decisions of This Court.

The Court of Appeal decision utilized a "per se" standard which would strike down any state statute differentiating between interstate and foreign commerce, no matter how reasonable the distinction. Such interpretation is in contrast to the modern trend of decisions allowing greater latitude to the states in instituting taxing policies.

In *Michelin Tire Corp. v. Wages,* 423 U.S. 276 (1976), this Court overruled *Low v. Austin,* 80 U.S. (13 Wall.) 29 (1872), holding that nondiscriminatory ad valorem property taxes did not constitute an impost or expost under Article I, Section 10, Clause 2 of the U.S. Constitution.

In *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977), this Court overruled *Spector Motor Service v. O'Connor,* 340 U.S. 602 (1951), and held that a state, under appropriate conditions, may tax directly the privilege of conducting interstate business.

In *Washington Revenue Dept. v. Assoc. of Washington Stevedoring Companies,* 435 U.S. 734 (1978), this Court overruled *Puget Sound Stevedoring Co. v. Tax Commissioner,* 302 U.S. 90 (1937), and put to rest the direct/indirect test, and reiterated the necessity to balance the burden placed on interstate commerce by the benefits to the State. This Court stated: "Respondents, therefore, have demonstrated no impediment imposed by the tax upon the regulation of foreign trade by the United States." (435 U.S. 754).

In *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 (1978), a single factor sales formula used to determine the amount of income tax attributable to the State was upheld. This Court pointed out that states have wide latitude in the selection of appropriate formulas which would only be disturbed in the event of clear evidence that the income attributed to the State was out of proportion to the business conducted.

In *Boston Stock Exchange v. State Tax Comm'r.,* 429 U.S. 318 (1977), this Court invalidated a New York tax scheme which was designed to provide a commercial advantage to local businesses (the New York Stock Exchange) to the detriment of out-of-state stock exchanges. The Court, however, cautioned:

> "On various occasions when called upon to make the delicate adjustment between the national interest and free and open trade and the legitimate interest of the individual States in exercising their taxing powers, the Court has counseled that the result turns on the unique characteristics of the statute at issue and the particular circumstances in each case." (429 U.S. 329).

The statute involved in the instant case makes no distinction between out-of-state and in-state residents or businesses. On the contrary, both are given the economic advantage of utilizing the Free Port Law if their goods qualify. There was no evidence or finding of interference with commerce. The Court of Appeal assumed that any distinction had an effect on interstate commerce, and applied a "per se" standard on the grounds that any interference or potential interference constituted an impermissible burden under the Commerce Clause. This case therefore raises an important issue concerning the limitations imposed by the Commerce Clause on the power of a state to enact tax statutes to meet local needs.

The inventory in the instant case had come to rest in California, and was not still in transit for purposes of prohibiting taxation under the Commerce Clause. Such goods were therefore part of the mass of goods in the State of California, subject to ad valorem property taxes under *Michelin v. Wages, supra* and the State may require that they participate and bear their fair share of local services. However, unlike the issue in *Michelin v. Wages,* the question now is whether the State *must* tax such inventory together with all other inventory in the State.

This is the first instance Amicus have been able to find in which a state exemption statute has been struck down as placing an unconstitutional burden on interstate commerce. There was no attempt in the decision to determine whether the supposed burden was either substantial or unreasonable. (*Richfield Oil Corp. v. State Board of Equalization,* 329 U.S. 69 (1946).)

In holding Section 225 unconstitutional the Court of Appeal cited *Boston Stock Exchange v. State Tax Comm'r., supra,* and *Michelin Tire Corp. v. Wages, supra.* These cases are distinguishable, and do not support the Court's decision. To the extent that these cases have applied constitutional principles on a case-by-case basis, they are contrary to the "per se" ruling of unconstitutionality in the instant case.

B. Review by This Court Is Warranted to Resolve a Conflict Between State Court Decisions With Respect to the Constitutionality of "Free Port Laws."

It is common practice for states to encourage local industry by providing tax exemptions. Examples are domestic wines while aging in California, dairy products in Wisconsin, certain fish products in Louisiana, and wheat products in the Midwestern states. With increasing frequencies states have been providing exemptions to inventories, and especially inventories stored for transshipment. "Not only are inventories exempt in the few but very important states that exempt all personal property . . . but they are wholly or partially exempt in numerous other states and are almost universally exempt if they have been brought into a state for storage or other limited activities before being shipped out of the state." (National Tax Journal, Property Tax Developments: Modernization, Classification, Site Value Taxation, 19:322, 324 (Sept. 1976).)

Such classification statutes are tested under Equal Protection principles. In the instant case the California Court of Appeal conceded that if Los Angeles County were only invoking an Equal Protection argument, it could not prevail, since a rational basis existed for the distinction. (85 Cal.App.3d at 777).

Over 35 states have some type of free port exemption. A substantial number of these statutes grant out-of-state or foreign products an exemption which is denied to similar products manufactured or grown in the United States or in the state in question. These distinctions are based on the origin of the goods, the same distinction struck down in the instant case. An appendix of free port laws is attached as Exhibit "D" hereto.

Amicus knows of no other instance in which a free port statute has been held unconstitutional.

In *Appeal of Martin* (S.Ct. N.C., 1974) 209 S.E.2d 766, the Court upheld a statute providing the following exemptions:

1. Cotton, tobacco, other farm products, goods, wares and merchandise held for shipment to any foreign country or stored at a seaport awaiting further shipment *after being imported from a foreign country.*

2. Personal property of nonresidents in their original package shipped into the state and placed in a public warehouse for the purpose of transshipment to a destination either outside of the state or within the state.

3. Personal property of residents in their original package placed in a public warehouse for transshipment, but only to an out-of-state destination. (G.S. §105-281 (1969) Cum.Supp.)[1]

The statute discriminated based on the origin of the goods and based on the residence of the owner of the goods. The statute specifically described its purposes:

> "It is hereby declared to be the policy of this state to use its system of property taxation in such manner, through the classification of the aforementioned property, *as to encourage the development of the ports of North Carolina . . .* [and] *to encourage the development of the State of North Carolina as a distribution center.*" (Emphasis added.)

[1]Under this statute a distributor such as Petitioner or either individual amicus, who warehouse in non-public facilities would: (a) be taxed on goods purchased domestically; (b) be given an exemption on imported goods. This is the same distinction struck down in the instant case.

In *State Bd. of Tax Comm'rs. v. Carrier Corp.* (S.Ct. Ind., 1977) 365 N.E.2d 1385, ad valorem property tax exemptions were upheld under a statute almost identical to the one reviewed in *The Appeal of Martin.* In a Petition for Rehearing the Court held that the statute did not unreasonably burden interstate commerce. (*State Bd. of Tax Comm'rs. v. Carrier Corp.* (S.Ct. Ind., 1977) 365 N.E.2d 1153.)

If, in the instant case, the Court of Appeal has accurately interpreted *Boston Stock Exchange* and *Michelin Tire Corp.*, then both the North Carolina and Indiana taxing schemes would also have to fail for violating the Commerce Clause. Undoubtedly many of the other taxing schemes listed in Exhibit "D" would similarly fail the Court of Appeal's test.

In *Nash Sales v. City of Milwaukee* (S.Ct. Wisc., 1929) 224 N.W. 126, the State Legislature, concerned about the competitive position of its warehousing industry, granted an exemption to property manufactured or produced *outside* of the state, and in storage in Wisconsin. The Court held that there was no violation of the Commerce Clause, stating:

> " 'The discretion of the Legislature in this field is so broad that it is not competent for the court to mark the constitutional limitations of it other than at the farthest one might go without transcending all reason.' [citation]" (at 129.)

In *Allied Stores of Ohio v. Bowers,* 358 U.S. 522, 3 L.Ed.2d 480, 79 S.Ct. 437 (1959), an Ohio statute exempted merchandise belonging to nonresidents held in storage but taxed similar property belonging to residents. This Court upheld the statute against Equal Protection arguments.

In *Raley & Bros. v. Richardson,* 264 U.S. 157 (1924), this Court upheld a Georgia tax upon brokers or commission merchants dealing in intrastate goods, which tax was not imposed upon similar brokers dealing in goods in interstate commerce. This Court rejected arguments that such distinction violated the Commerce Clause.

Summary.

The shield of the Commerce Clause is generally sought by taxpayers attempting to prevent state and local taxation. Rarely if ever has such shield been successfully invoked by a taxing subdivision of the state to attack the state's own taxing scheme.

In *Boston Stock Exchange, supra,* this Court struck down, on Commerce Clause grounds, a New York taxing scheme providing benefits to residents, to the detriment of nonresidents. In *Allied Stores of Ohio, supra,* this Court upheld an Ohio statute providing a tax benefit to nonresidents to the exclusion of residents, attacked on the basis of Equal Protection.

In the instant case no distinction is made between residents and nonresidents; each are afforded the benefits of the transshipment exemption. The statute in question merely provides an exemption to one *type* of goods, to wit, goods which had been imported from abroad.

In *Japan Line, Ltd. v. County of Los Angeles,* ..... U.S. ..... (1979), this Court held that California property tax applied to foreign owned instrumentalities of international commerce prevented the Federal Government from speaking with one voice in international trade. In contrast, in the instant case the goods which are exempted have come to rest in California, are

part of the mass of goods located in the state, and are fully subject to the power of the state. (*Michelin Tire v. Wages, supra.*) The risk that foreign commerce will be burdened by the instant exemption is so remote that it can be said to be nonexistent. (*Bob-Lo Excursion Co. v. Michigan,* 33 U.S. 28 (1948).)

To allow the California Court of Appeal decision to stand would place in jeopardy free port or transshipment statutes throughout the nation, it would question every local statute attempting to encourage public policy or local economic goals by providing benefits to one type of activity or product while denying them to other activities or products. The decision is in conflict with the results and reasoning of *Michelin v. Wages, Complete Auto Transit, Inc. v. Brady, Washington Rev. Dept. v. Stevedoring Ass'n, Boston Stock Exchange v. State Tax Comm'r,* and *Raley & Bros. v. Richardson.*

Conclusion.

For the foregoing reasons the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

GERALD T. MANPEARL,
Attorney for Amicus Curiae.

BAKER, ANCEL, REDMOND & HALL,
and
EVANS, MANPEARL & HARTER,
Of Counsel.

EXHIBIT A.

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Wilshire Boulevard at Grand Avenue
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April 12, 1979

Gerald T. Manpearl, Esq.
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350 So. Figueroa St., Suite 900
Los Angeles, California 90071

Re: Sears, Roebuck & Co. v. County of Los Angeles (Zee Toys v. County of Los Angeles, 85 Cal.App.3d 763 (1978).)

Dear Mr. Manpearl:

This will confirm our telephone conversation of yesterday to the effect that we have no objection to your filing, by your firm and Baker, Ancel, Redmond & Hall, an Amicus Curiae Brief on behalf of the Petitioner Sears, Roebuck & Co. in support of the Petition for Writ of Certiorari to the Court of Appeal of the State of California, Second Appellate District, which Petition is being filed by our office with the United States Supreme Court.

Sincerely,

/s/ Frank M. Keesling
Frank M. Keesling
Of Loeb and Loeb

EXHIBIT B.

COUNTY OF LOS ANGELES
OFFICE OF THE COUNTY COUNSEL
648 Hall of Administration
Los Angeles, California 90012
John H. Larson, County Counsel

April 12, 1979

Gerald T. Manpearl, Esq.
Evans, Manpearl & Harter
350 So. Figueroa St., Suite 900
Los Angeles, California 90071

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Very truly yours,
JOHN H. LARSON
County Counsel
/s/ By James Dexter Clark
JAMES DEXTER CLARK
Deputy County Counsel

EXHIBIT C.

[1]"Section 225. Personal property manufactured or produced (1) outside this state and brought into this state for transshipment out of the United States, or (2) outside of the United States and brought into this state for transshipment out of this state, for sale in the ordinary course of trade or business shall be exempt from taxation. The exemption under this section shall not apply to personal property in manufacturing process or production. Such process or production shall not include the breaking in bulk, labeling, packaging, relabeling, or repackaging of such property.

"Section 225.1 A person claiming an exemption under Section 225 may either claim this exemption by (1) a percentage method of determining property held for transshipment on hand at a particular location by allocating a portion of the total inventory, using the percentage determined by dividing the total out-of-state shipments by the taxpayer from that location during the preceding year by the total of such shipments from that location during such year, or (2) an actual method as evidenced by contracts of sale on the tax lien date, and a full, true and correct inventory of all property held for transshipment together with the date of receipt of the same, the date of withdrawal of the same, the point of origin thereof, and the point of ultimate destination thereof.

"Section 225.2. Any property exempted under Section 225 which is reconsigned to a final destination in this state shall be subject to escape assessment procedures."

EXHIBIT D.

[1]The following statutes exempt goods shipped into and stored in the state from outside the state, awaiting shipment out of the state. Similar goods manufactured or produced in the state are not exempt: Ariz.Rev.Stat. §42-631; Iowa Code Ann. §427.16; La.Rev.Stat.Ann. 47:1951.3; Minn.Stat.Ann. §272.022; Mo.Rev. Stat. §137.093 (Vernon); Mont.Rev.CodesAnn. §84-202, Repl. Vol. 5 (Part 2); Nev.Rev.Stat. §361.160; 68 Okla.Stat.Ann. Tit. 68 §2425(e) (West); Or.Rev.Stat. §307.810; S.C. Code §12-1-50; Tenn.Code Ann. §67-518; and Tex. Tax Code Ann. Tit. 122, §7150(f) (Vernon's).

The following statutes exempt goods shipped into and stored in the state from outside the state, awaiting shipment either in or out of the state, as well as goods manufactured or produced in the state stored awaiting shipment out of the state. Similar goods manufactured or produced in the state stored awaiting shipment in the state are not exempt; Conn.Gen.Stat.Ann. §12-95(a); Ill.Stat.Ann. Ch.120, §500.21 (Smith-Hurd); Kan.Stat.Ann. §79-201(f); Ky.Rev.Stat. §132.-095; N.C.Gen.Stat. §105-275(10) (1977 Supp); and Wisc.Stat.Ann. §70.111 (West).

The following statutes exempt goods shipped into and stored in the state from outside the state awaiting shipment either in or out of the state. Similar goods manufactured or produced in the state are not exempt: Ind.Code. §6-1.1-10-29; and Mass.Gen.Laws Ann. Ch. 59, §2.

Ga.Code Ann. §92-186, 187, exempts goods originating in foreign countries stored in the port of entry in Georgia awaiting shipment outside of the state. Similar goods originating in Georgia or in other states stored in Georgia awaiting shipment out of the state are not exempt.

[2]See R&T Code §992, providing an exemption to wine and brandy in bond during the aging process, except for the first year. This exemption is only provided if the wine or brandy is produced or manufactured in California, and a similar exemption is not provided to imported wine or brandy. See, *e.g.*, R&T Code §232, providing an exemption to cargo containers used for transportation of cargo by vessels in ocean commerce. Unaffected are cargo containers used for rail, air or truck transportation; R&T Code §220, exempting aircraft brought into California for repair but not other aircraft in California which is being repaired.